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In The

Supreme Court of the United States

October Term, 1998

AMERICAN MANUFACTURERS MUTUAL INSURANCE COMPANY, *et al.*,

Petitioners,

v.

DELORES SCOTT SULLIVAN, *et al.*,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals for The Third Circuit

BRIEF OF RESPONDENTS

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QUESTIONS PRESENTED

1. Whether insurance companies were "state actors" when, acting in conjunction with a state agency, they used statutory provisions authorizing them to stop workers' compensation medical benefits that were disabled workers' legally exclusive source of medical benefits?

2. Whether due process requires that disabled workers receive prior notice and an opportunity to be heard before their workers' compensation medical benefits can be indefinitely suspended pending utilization review and administrative hearings?

TABLE OF CONTENTS

Page

Counterstatement 1

History and Scope of the Workers' Compensation Act 4

The Operation of the Workers' Compensation System.. 7

Baksalary v. Smith Holds Automatic Supersedeas Unconstitutional..... 8

Medical Disputes Prior to Act 44..... 9

The Passage of Act 44..... 10

District Court Proceedings..... 13

The Appellate Proceedings 15

I. Introduction and Summary of Argument 16

II. The Third Circuit Correctly Held That the Utilization Review Provisions Violated Due Process 19

III. Plaintiffs' Facial Challenge Renders the Discrete Tests Inapplicable and Directly Implicates the State in the Decision to Stop Medical Benefits 24

A. A Totality of the Circumstances Approach Should Be Used to Find State Action Where There Is No Facial Constitutional Challenge..... 31

1. *Edmonson's* Totality Test..... 31

2. Application of the Totality Test to the Employer's Role in Utilization Review... 33

a. Governmental Assistance and Benefits .. 33

b. Traditional Government Function 35

TABLE OF CONTENTS – Continued

Page

c. Aggravation by Unique Incidents of Governmental Authority..... 38

d. The Third Circuit Properly Applied the *Edmonson* Factors 40

B. Even If Discrete Tests Are Required, the Third Circuit's State Action Holding Against the Insurers Should Be Affirmed 40

1. Joint Participation/Symbiotic Relationship Test..... 40

2. The Public Function Test 44

3. Government compulsion and Encouragement..... 47

Conclusion..... 50

TABLE OF AUTHORITIES

Page

CASES

Arizona v. California, 460 U.S. 605 (1983) 21

ADIA Personnel Agency v. Workers Compensation Appeal Board, 137 Pa.Cmwlth. 405 (1991) 10

Alliance For Community Media v. F.C.C., 10 F.3d 812 (D.C. Cir. 1993)..... 18, 30, 48, 50

Baksalary v. Smith, 579 F. Supp. 218 (E.D. Pa. 1984), *appeal denied*, 469 U.S. 1146 (1985), *aff'd*, 772 F.2d 893 (3d Cir. 1985)..... 8, 9

Baksalary v. Smith, 591 F. Supp. 1218 (E.D. Pa. 1984) 9, 10, 31, 39, 46, 47

Bayless v. Philadelphia National League Club, 472 F. Supp. 625 (1979), *aff'd*, 615 F.2d 1352 (1980) 5

Bell v. Burson, 402 U.S. 535 (1971) 21

Bible v. Com., Dept. of Labor & Ind., 548 Pa. 247 (1997)..... 6

Blum v. Yaretsky, 457 U.S. 991 (1982) 18, 43, 47

BMW of North America, Inc. v. Gore, 517 U.S. 559 (1996)..... 25

Boddie v. Connecticut, 401 U.S. 371 (1971) 20

Burton v. Wilmington Parking Authority, 365 U.S. 715 (1961)..... 32, 40, 41, 43, 44

Cleveland Board of Education v. Loudermill, 470 U.S. 532 (1985)..... 21

Cohen v. Cowles Media Co., 501 U.S. 663 (1991)..... 25

TABLE OF AUTHORITIES – Continued

Page

Connecticut v. Doehr, 501 U.S. 1 (1991) 20, 21, 23

Edmonson v. Leesville Concrete Co., Inc., 500 U.S. 614 (1991)..... *passim*

Evans v. Newton, 382 U.S. 296 (1966) 29, 31

Ex Parte Virginia, 100 U.S. 339 (1879) 24

Flagg Brothers, Inc. v. Brooks, 436 U.S. 149 (1978) 18, 29, 44, 49

Fuentes v. Shevin, 407 U.S. 67 (1972)..... 17, 21, 23

Gallagher v. Neil Young Freedom Concert, 49 F.3d 1442 (10th Cir. 1995)..... 45

Garcia v. San Antonio Metropolitan Transit Authority, 469 U.S. 528 (1985)..... 45

Goldberg v. Kelly, 397 U.S. 254 (1970) 21

Goss v. Lopez, 419 U.S. 565 (1975)..... 21

Hall v. Beals, 396 U.S. 45 (1969)..... 3

Hankee v. Wilkes-Barre/Scranton Int'l Airport, 532 Pa. 494 (1992)..... 6

Henderson v. Workers' Compensation Appeal Board, 69 Pa.Cmwlth. 613 (1982) 46

Jackson v. Metropolitan Edison Co., 419 U.S. 345 (1974)..... 18, 47, 49

Joint Anti-Facist Refugee Committee v. McGrath, 341 U.S. 123 (1951)..... 39

TABLE OF AUTHORITIES – Continued

Page

Keller v. Old Lycoming Township, 286 Pa. Super. 339 (1981) 6

Krawchuk v. Philadelphia Electric Co., 497 Pa. 115 (1981) 4

Lebron v. National Railroad Passenger Corp., 513 U.S. 374 (1995) 18, 29

Logan v. Zimmerman Brush Co., 455 U.S. 422 (1982) 1, 20, 21, 24, 31, 37

Lugar v. Edmondson Oil Co., 457 U.S. 922 (1982) 32, 41, 43, 44

Mark v. Borough of Hatboro, 51 F.3d 1137 (3d Cir. 1995) 44

Mathews v. Eldridge, 424 U.S. 319 (1976) 1, 21, 22, 23, 24

McKeesport Hospital v. Accreditation Council, 24 F.3d 519 (3d Cir. 1994) 44

Memorial Hospital v. Maricopa County, 415 U.S. 250 (1974) 22

Memphis Light, Gas & Water Div. v. Craft, 436 U.S. 1 (1978) 20, 21

Moose Lodge No. 107 v. Irvis, 407 U.S. 163 (1972) 47

Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306 (1950) 21

Muskrat v. U.S., 219 U.S. 346 (1911) 3

TABLE OF AUTHORITIES – Continued

Page

NAACP v. Claiborne Hardware Co., 458 U.S. 886 (1982) 25

National Collegiate Athletic Association v. Tarkanian, 488 U.S. 179 (1988) 35

New York Times Co. v. Sullivan, 376 U.S. 254 (1964) 16, 17, 24, 25

Nixon v. Condon, 286 U.S. 73 (1932) ... 16, 17, 18, 25, 29, 31

Parratt v. Taylor, 451 U.S. 527 (1981) 20

Paul v. Watchtower Bible and Tract Society, 819 F.2d 875 (9th Cir. 1987) 24

Reitman v. Mulkey, 387 U.S. 369 (1967) ..... *passim*

Rendell-Baker v. Kohn, 457 U.S. 830 (1982) 18, 49

Richmond Newspapers, Inc. v. Virginia, 448 U.S. 555 (1980) 39

Rumph v. SWIF, 964 F. Supp. 180 (E.D. Pa. 1997) 2

San Francisco Arts and Athletics, Inc. v. United States Olympic Committee, 483 U.S. 522 (1987) 46

Silas v. Smith, 361 F. Supp. 1187 (E.D. Pa. 1973) 46

Smith v. Allwright, 321 U.S. 649 (1944) 16, 17

Sniadach v. Family Finance Corp., 395 U.S. 337 (1969) 17

Stonebraker v. Workers' Compensation Appeal Board, 163 Pa.Cmwlth. 468 (1994) 22

Tulsa Prof'l Collection Services, Inc. v. Pope, 485 U.S. 478 (1988) ..... *passim*

TABLE OF AUTHORITIES – Continued

Page

United Auto Workers v. Gaston Festivals, Inc., 43 F.3d 902 (4th Cir. 1995) 44

United States v. Classic, 313 U.S. 299 (1941) 39

West v. Atkins, 487 U.S. 42 (1988) ..... *passim*

Winterberg v. Transportation Insurance Co., 72 F.3d 318 (3d Cir. 1995) 5, 6

Zinermon v. Burch, 494 U.S. 113 (1990) 1, 20

STATUTES AND REGULATIONS

Federal Rules of Civil Procedure 12(b)(6) 14, 50

28 U.S.C. § 2281 8

42 U.S.C. § 1983 1

34 Pa. Code 121.1 7

77 Pa.Stat.Ann. § 1 *et seq.* 1

77 Pa.Stat.Ann. § 53 9

77 Pa.Stat.Ann. § 413(a) 8, 9, 46

77 Pa.Stat.Ann. § 461 5

77 Pa.Stat.Ann. § 481(a) 5, 7

77 Pa.Stat.Ann. § 501 5

77 Pa.Stat.Ann. § 501(a)(1) 5

77 Pa.Stat.Ann. § 531 10

77 Pa.Stat.Ann. § 531(3)(i) 6, 7

77 Pa.Stat.Ann. § 531(5) ..... *passim*

TABLE OF AUTHORITIES – Continued

Page

77 Pa.Stat.Ann. § 531(6) ..... *passim*

77 Pa.Stat.Ann. § 531(6)(ii) 12

77 Pa.Stat.Ann. § 701 7

77 Pa.Stat.Ann. § 711 7

77 Pa.Stat.Ann. § 717.1 ..... 7, 8

77 Pa.Stat.Ann. § 715 7

77 Pa.Stat.Ann. § 731 ..... 7, 8

77 Pa.Stat.Ann. § 751 8

77 Pa.Stat.Ann. § 991 ..... 8, 12

77 Pa.Stat.Ann. § 1055 5

OTHER AUTHORITIES

Brest, State Action and Liberal Theory: A Case Note on *Flagg Brothers v. Brooks*, 130 Pa. L. Rev. 1296 (1982) 17

ten Broek, The Disabled and the Law of Welfare, 54 Cal. L. Rev. 809 (1966) 6

Strickland, The State Action Doctrine and the Rehnquist Court, 18 Hastings Const. L. Q. 587 (1991) 24, 25, 32

Krotoszynski, Back to the Briar Patch: An Argument in Favor of Meta-Analysis in State Action Determinations, 94 Mich. L. Rev 25

BLACK'S LAW DICTIONARY, 4th Ed. (1951) 13

COUNTERSTATEMENT

This case presents a direct constitutional challenge to the utilization review procedures enacted in 1993 by the Pennsylvania legislature to amend its Workers' Compensation Act.[1] Those procedures permitted insurers or self-insured employers (hereafter "Petitioners" or "employers") to stop or supersede the workers' compensation medical benefits of thousands of injured workers, in which the workers have an undisputed property interest, without notice and with no pre-deprivation opportunity to be heard. These amendments were part of a legislative package directed at cost containment known commonly as "Act 44".

The Respondents in this case, the Plaintiffs below (hereafter "Plaintiffs" or "injured workers"), contended that the state, which administers the benefit program and has exclusive control over the resolution of disputes among the parties, violated their right to due process of law under the Fourteenth Amendment and 42 U.S.C. § 1983 when it established the procedures contained in § 306 (f.1)(5) and (6) of the Act, which delegated to the employers the power and authority to supersede an injured workers' medical benefits without any pre-deprivation notice or opportunity to be heard. *Zinermon v. Burch*, 494 U.S. 113 (1990); *Logan v. Zimmerman Brush Co.*, 455 U.S. 422 (1982); *Mathews v. Eldridge*, 424 U.S. 319 (1976).[2] Plaintiffs also sued ten named insurance carriers, contending that they were state actors in the context of the statutory scheme and therefore liable to plaintiffs for the violation of their due process rights.

The Third Circuit Court of Appeals found the Commonwealth defendants below constitutionally liable to Plaintiffs for their role in enacting and administering the challenged provisions. It further held that the employers and insurers who use the utilization review

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[1] Pa. Stat. Ann. tit.77, Sec. 1 *et seq.*, Act of June 2, 1915, P.L. 736.

[2] In bringing this challenge, Plaintiffs sued numerous state officials responsible for implementation and administration of the law as well as the ten insurers named as Petitioners in this case, who have assumed the employers' responsibilities and immunities under the terms of the Act. Plaintiffs also sued the School District of Philadelphia, representing self-insured Pennsylvania employers.

provisions to stop an injured worker's vested medical benefits pending resolution of the utilization review and appellate process, a process which can take months or years to complete, are state actors when they use those provisions.[3] In reaching this conclusion, the Third Circuit applied a flexible approach that viewed the decision to invoke utilization review in the context of the overall statutory scheme, and focused on the importance of the public benefit at issue. The court recognized the integral role that the employer plays in delivering this public benefit, and the close systemic relationship between the state and the employers in the context of utilization review, which the court found is a state created and administered mechanism that empowered the employer to supersede the public entitlement. The Third Circuit held that the Commonwealth defendants and the insurers, who are the Petitioners here, were jointly liable to Plaintiffs for the violation of their constitutional rights.[4]

Although the Commonwealth defendants filed a Conditional Cross Petition for Writ of Certiorari as to the Third

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[3] Insurers stand in the shoes of the employers, whose liability they assume, for purposes of the Act. Because there is no meaningful distinction between them, most references will be to employers, unless the Petitioners themselves are being discussed.

[4] Because of the way the Third Circuit disposed of the state action issue, it was not forced to confront the equal protection issue which would have arisen had it decided that the law violated the due process clause but that the private insurers and self-insured employers using the law were not state actors. Pet.App. at 25a. The equal protection problem would arise because it is undisputed that the State Workers' Insurance Fund ("SWIF"), which provides workers' compensation coverage not only to public employers in Pennsylvania, but to a wide array of private employers as well, is a state actor. *Rumph v. SWIF*, 964 F. Supp. 180 (E.D. Pa. 1997). *See also* Petitioner's Brief, 30 n.15. Under these circumstances an employee whose workers' compensation coverage is funded through SWIF would be afforded the protections of the due process clause, whereas an employee whose coverage is funded through a private insurer would not. There is no rational basis for such a distinction, and it could not withstand an equal protection challenge. It would also wreak havoc in Pennsylvania's workers' compensation system.

Circuits' holding against them, that petition was denied by this Court. Subsequent to the Third Circuit's decision, the Bureau changed its procedures to ensure that injured workers subject to utilization review are provided with a notice which informs them of their opportunity to submit a written statement to the utilization reviewer and that if the review is adverse, their medical benefits may be lost.[5] The Plaintiffs' case against the Commonwealth, therefore, is over and the Commonwealth defendants are not participants in these proceedings.

Because the due process issue has been resolved through the Third Circuit's holding against the Commonwealth and the Commonwealth's modification of its procedures, the only issue which requires the Court's decision is whether the Third Circuit properly held that insurers who invoke utilization review and stop the medical benefits of injured workers are state actors. To the extent that the Petitioners seek a ruling on the due process issue, they are requesting an advisory opinion which does not comport with the scope of this Court's jurisdiction under Article III of the United States Constitution.[6] *Muskrat v. United States*, 219 U.S. 346 (1911). The insurers are seeking a declaration from this Court that the right to stop the medical benefits of an injured worker, a right no longer

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[5] Joint Appendix, hereafter "Jnt. App.", at 50.

[6] The provision challenged in Plaintiffs' Amended Complaint states: "All payments to providers for treatment provided pursuant to the Act shall be made within thirty (30) days of receipt of such bills and records unless the employer or insurer disputes the reasonableness or necessity of the treatment provided pursuant to paragraph (6)" (relating to utilization review). The Third Circuit struck the "unless" clause from the statute because it allowed the employers to stop a public benefit without notice or an opportunity to be heard. Without the "unless" clause, there is no mechanism left in the statute that would allow the employers to supersede an injured worker's benefits. The Commonwealth is not defending the pre-*Sullivan* statute, and the Petitioners' due process position, therefore, raises important mootness questions. *Hall v. Beals*, 396 U.S. 45. 48 (1969).

conferred upon them by Pennsylvania law, would be constitutional should the state later decide to restore it.[7] Such a request is inappropriate and should be denied.

History and Scope of the Workers' Compensation Act

The Pennsylvania's Workers' Compensation Act (hereafter "the Act"), was passed in 1915 to compensate workers for disabilities or death suffered as a result of work-related injuries or occupational diseases. Prior to the enactment of the legislation, injured workers and their survivors could litigate claims against their employers for damages, including lost wages, medical costs, pain and suffering and other traditional tort remedies. However, because this was an action in tort, workers who failed to prove employer negligence were left with no remedy at all. *See Krawchuk v. Philadelphia Electric Co.*, 497 Pa. 115 (1981).

The Act reflected a major compromise in the interests of both employers and employees. In exchange for the guarantee

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[7] Petitioners' due process challenge is incomprehensible as it confuses their request for a prospective advisory ruling with the remedy which should flow from their past use of the unconstitutional procedures. The Third Circuit's ruling as to the state's notice procedures and its requirement that Plaintiffs be given an opportunity to be heard were premised upon the duty of the Commonwealth to provide procedural protections *before* the deprivation of benefits took place. The Petitioners have not challenged the Third Circuit's holding that the lack of notice and opportunity to be heard in the state's procedures rendered the statute unconstitutional. *See Petitioner's Brief at 30.* Having conceded that the lower court's constitutional ruling as to notice and opportunity to be heard were correct, their contention here that the pre-deprivation supersedeas would be constitutional, if it still existed, makes no sense. If the statute was unconstitutional as presented to the Third Circuit, the only issue properly before the Court is whether the Petitioners were state actors when they invoked it. The inquiry as to whether the supersedeas of benefits by them pursuant to the procedures as modified by the state would make them liable for the constitutional violation prospectively has nothing to do with whether they are liable to Plaintiffs for the deprivation which took place under the original statutory provisions, which concededly provided neither notice nor an opportunity to be heard.

of payment for wage loss and medical costs from injury regardless of fault, the employee forfeited her constitutional right to sue her employer in tort. *Winterberg v. Transportation Insurance Co.*, 72 F.3d 318 (3d Cir. 1995). Workers' compensation became the exclusive remedy for work related injuries in Pennsylvania. 77 P.S. § 481; *Bayless v. Philadelphia National League Club*, 472 F. Supp. 625 (E.D. Pa. 1979), *aff'd*, 615 F.2d 1352 (3d Cir. 1980).[8]

In 1974, the Act was amended, making it *mandatory* for employers to provide workers' compensation coverage for their employees. Act of Dec. 5, 1974, P.L. 782, 784, Pa. Stat. Ann. tit. 77, § 461, 481(a). Under the Act, employers may satisfy their obligation to insure against their employees' work-related injuries or occupational diseases in one of three ways: (1) the employer may retain a "private" insurance carrier authorized by the Pennsylvania Insurance Department to sell or issue workers' compensation insurance in Pennsylvania; (2) the employer may insure itself through SWIF, a fund created by the General Assembly and administered by state employees and officers; or (3) the employer may self-insure. Any employer who fails to obtain coverage through one of these methods is subject to fines, imprisonment, or both. *Id.* at § 501. In the event that an employer cannot procure insurance coverage, the state, through SWIF, will provide the insurance itself. *Id.* In the event of insolvency the state provides benefits to injured workers through a state administered security fund. 77 Pa. Stat. Ann. § 1055.

Thus, the workers' compensation system is not a private insurance model. *Winterberg*, 72 F.3d 318, 325, n.4 (3rd Cir. 1995) (distinguishing workers' compensation from private insurance). Although private insurers and employers participate in the provision of benefits, the workers' compensation system in Pennsylvania is a comprehensive public benefit

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[8] Pursuant to the statute, the insurer not only assumes all of the employer's liability, but also, is "entitled to all of the employer's immunities and protection" under the Act. 77 P.S. 501(a)(1). Accordingly, an injured worker cannot sue the insurer for bad faith, a right he would have outside the context of the Act.

mechanism intended to fulfill important constitutional and statutory objectives.[9] Unlike under private insurance, the injured worker has a statutory right to have the wage and

[9] The Petitioners vigorously dispute that workers' compensation benefits in Pennsylvania are public benefits. They cite no legal authority for their contention, and rely upon patently inapt analogies to deny what has been explicitly stated by the Pennsylvania Supreme Court, *i.e.*, that workers' compensation benefits are not a matter of contract, but are provided as a statutory entitlement through the Commonwealth's police power. *Bible v. Department of Labor and Industry*, 548 Pa. 247 (1997); *Hankee v. Wilkes-Barre/Scranton Int'l Airport*, 532 Pa. 494 (1992). That workers' compensation benefits are public benefits as a matter of law is evident from the following: the right to workers' compensation is guaranteed to all workers in Pennsylvania who are not self-employed, and this guarantee is enforced by the state. Workers cannot bargain away their right to workers' compensation, and they may not opt out in favor of their own privately obtained coverage. A plaintiff aggrieved by the conduct of his employer or its insurer cannot drop his coverage and shop for a new carrier and he may not procure care for his injuries outside the provisions of the Act. 77 P.S. § 531(3)(i). He is not a party to any contract other than the one with his employer; moreover, the employer's duty to provide for workers' compensation does not emanate from a contract or insurance policy, but from state law; workers' compensation constitutes a *quid pro quo* for the right of workers to sue their employers for damages as a result of workplace injuries. It is the exclusive remedy for such injuries. *Winterberg, supra*. The private resolution of workplace injuries through civil litigation was replaced by a publicly administered Bureau which dictates the level of benefits to be paid, the circumstances under which benefits can be paid, as well as those under which they can be suspended and terminated. The Bureau is an integral participant in the statutory model. Workers' compensation has been deemed by the Pennsylvania Courts to be a public benefit, equivalent to "a soldier's right to a pension". *Keller v. Old Lycoming Township*, 286 Pa. Super. 339, 348 n.6 (1981). *See also* ten Broek, *Disability and the Law of Welfare*, 54 Cal.L.Rev. 809, 822 (1966) ("governmental discretion as to the amount, character, and conditions of aid, and governmental machinery and technical apparatus brought to bear upon the assessment of individual need, are prime characteristics of the system of public welfare").

medical coverage provided to him or her at no charge. This coverage is guaranteed by the Commonwealth, which vigorously enforces the entitlement through the Bureau of Workers' Compensation ("the Bureau").

Conversely, the injured worker has no right to opt out of the workers' compensation system, in favor of his own private insurance coverage or no coverage at all. 77 P.S. § 481(a). Moreover, the injured worker is statutorily prohibited from securing medical services for work-related injuries from his own funds. 77 P.S. § 531(3)(i). In addition, the employee has no right to choose the provider of his benefits. The employee is a captive of whatever carrier the employer contracts with, subject to the protections of the Act.

The Operation of The Workers' Compensation System

The Bureau works hand in hand with employers to provide benefits to injured workers. Whether benefits are paid by the employer directly, through SWIF, or by a commercial insurer, the Bureau is an integral participant in the operation of the statute. It actively enforces the Act's mandates and is authorized to ensure compliance by insurers through the assessment of monetary penalties for violation of its provisions. 77 P.S. § 701. Pursuant to its statutory authority, the Bureau has adopted regulations implementing the Act and has imposed numerous reporting requirements upon employers and insurers involved in the system. 34 Pa. Code § 121.1 *et seq*. For uniformity and ease of administration, the Bureau has developed numerous forms for each of these reporting requirements. Use of these forms is mandatory. 77 P.S. §§ 717.1, 711, 731.

The Bureau is more than a passive repository for completed forms, however. The mandated documents reflect the legal status of every injured employee. The Bureau not only collects these documents, but reviews them for compliance with the Act. 77 P.S §§ 715, 731. In the event of a dispute between the parties, these documents will provide the basis on which the state ultimately determines the injured worker's entitlement. 77 P.S. § 731. They also provide a foundation for enforcement actions against employers or insurance carriers

which the Bureau determines are in violation of the provisions of the Act. 77 P.S. § 991.

Baksalary v. Smith Holds Automatic Supersedeas Unconstitutional

From 1984, until the Pennsylvania Legislature passed Act 44, which encompasses the utilization review provisions at issue in this case, an employee eligible to receive workers' compensation benefits[10] could not have those benefits stopped without his consent, even temporarily, without an order from a workers' compensation judge. This was the result of a federal court order in *Baksalary v. Smith*, 579 F. Supp. 218 (E.D. Pa. 1984), *appeal denied*, 469 U.S. 1146 (1985) *aff'd*, 772 F.2d 893 (3d Cir. 1985). A unanimous three-judge panel[11] in *Baksalary* invalidated a portion of Section 413(a) of the Act, which had provided for the automatic cessation, or supersedeas, of workers' compensation benefits upon an employer's filing of an affidavit of recovery with the state workers' compensation authorities, accompanied by a physician's affidavit, or an affidavit that the worker had returned to work. A supersedeas invoked in this way would remain in effect throughout the litigation over whether the employee's

[10] Petitioners imply that the insured workers have obtained their current medical treatment with no screening process and that, therefore, the reasonableness and necessity of the treatment has never been ascertained, to the unfair detriment of the insurers. This is not the case. A person can become entitled to workers' compensation benefits either by voluntary agreement between the parties or the unilateral acknowledgment by the employer that the injury is compensable. Alternatively, eligibility can be established through a favorable decision by a workers' compensation judge after extensive hearings. 77 P.S. § 717(1), 731, 751. Each of the named plaintiffs and each member of the class they seek to represent have become entitled to receive workers' compensation medical benefits through one of these mechanisms. They are not applicants, but pursuant to the terms of the Act, have been determined eligible for the medical benefits they were receiving at the time those benefits were stopped.

[11] *Baksalary* was decided by a three judge court convened under 28 U.S.C. § 2281, *repealed* Pub. L. 94-381, §§ 1, 2 *effective* Aug. 12, 1976, 90 Stat. 1119.

right to benefits should be permanently terminated or suspended.

The *Baksalary* court held that the automatic supersedeas provision contained in Section 413(a) was unconstitutional because it deprived injured workers of a property right in their workers' compensation benefits without notice or an opportunity to be heard. In reaching that decision, the court held that insurers and self-insured employers were state actors for purposes of the Fourteenth Amendment when they invoked the automatic supersedeas provision of Section 413(a). This was based upon the formal and systematic participation of state personnel which was triggered by the employer's invocation of supersedeas in each case.

The *Baksalary* decision was followed by a consent decree that eliminated the automatic supersedeas provision of Section 413(a). *Baksalary v. Smith*, 591 F. Supp. 1218 (E.D. Pa. 1984). Unless an injured worker returned to work with no wage loss, there was no remaining provision in the Act by which an automatic and unilateral cessation of workers' compensation benefits could be achieved. All terminations of benefits, even temporary ones, were required to be preceded by fair notice and a hearing.[12]

Medical Disputes Prior to Act 44

After *Baksalary* and before the passage of Act 44, all disputes about medical treatment were completely protected from unilateral cessation by an employer or insurer. Disputes as to the reasonableness and necessity of the treatment, (the focus of utilization review), were exclusively resolved by petition filed with the Bureau and assigned to a workers' compensation judge. There was no provision for supersedeas

[12] The automatic supersedeas invalidated in *Baksalary* operated upon both wage loss and medical benefits. Where medical benefits were the only issue being contested, § 413(a) did not apply. Such reviews were conducted pursuant to Section 306(f), which specifically prohibited the supersedeas of those benefits while under review, automatically or otherwise. 77 P.S. § 53.

of medical treatment pending review.[13] Injured workers were given the opportunity to appear at hearings and testify on their own behalf. They had the right to be represented by counsel. They had the opportunity to present medical evidence and cross examine the employer's medical expert. With the closing of the record, the Judge would issue a decision containing findings of fact and conclusions of law based on the evidence. If the Judge ultimately decided that the treatment was reasonable, the injured worker would continue to receive it without an interruption in service. If not, the insurer would be relieved of the obligation of further payment, and would be reimbursed by a state supersedeas fund for payments which had been made for treatment deemed unreasonable. *ADIA Personnel Agency v. Workers Compensation Appeal Board, supra.*

The Passage of Act 44

In June 1993, in response to political pressure from employers and insurance carriers about the rising cost of medical treatment, the Pennsylvania General Assembly passed a measure known as Act 44, which set forth provisions for medical cost containment, including the utilization review provisions at issue here. Section 306(f.1)(5), like the provision invalidated in *Baksalary*, operates upon injured workers whose eligibility to receive workers' compensation benefits, including medical treatment, has already been established. 77 P.S. § 531(5). It provides a mechanism for employers to stop the medical component of those benefits without any showing of medical justification, with no prior notice to the injured

[13] The pre-Act 44 Section 306(f)(2)(II), 77 P.S. § 531, stated, "The employer shall have the right to petition the department for review of the necessity or frequency of treatment . . . Such a petition shall in no event act as a supersedeas, and during the pendency of any such petition, the employer shall pay all medical bills if the physician or other practitioner of the healing arts files a report or reports as required [by the Act]." *See also ADIA Personnel Agency v. Workers Compensation Appeal Board*, 137 Pa.Cmwlth. 405 (1991) (workers' compensation referee had no authority to order discretionary supersedeas of challenged medical benefits pursuant to Section 306(f)).

worker or any opportunity to respond, upon the filing of a request for utilization review with the Bureau and subject to the Bureau's acceptance of the request. The Bureau refers requests for utilization review to Utilization Review Organizations ("URO's"), which are approved, trained and supervised by the Bureau. The URO's review the challenged treatment, and determine whether the medical benefits at issue must be paid.

The Bureau serves the dual function of gatekeeper and traffic cop for the utilization review process. Access to the utilization review system can only be invoked by filing a form devised by the Bureau for that purpose. Employers are empowered by the statute, upon approval by the state, which reviews the form to determine if the request is proper and submitted in timely fashion, to stop payments for challenged medical treatment. In order to maintain the supersedeas, the request for utilization review must be accepted by the Bureau. If it is, the supersedeas may extend throughout the review process, which can take months, or even years, to complete. If the request is not approved, the supersedeas is rescinded. There are numerous reasons that a request for utilization review can be rejected by the Bureau.[14] The Bureau rejects requests for review twenty per cent of the time. Third Cir. App. at C-50.

Absent a sufficient and proper request to the Bureau for utilization review, the medical benefits at issue must be paid

[14] These include: failure of an insurer or employer to accept liability for the work-related injury; failure to certify proof of service, to sign the request, to identify the type of treatment or procedure to be reviewed, or to provide information needed by the Bureau to process the request; the form is also rejected if there is pendency of the same issue before the peer review authorities by request of a workers' compensation judge; because the request seeks review of treatment that occurred before August 31, 1993, or seeks review of the relatedness of treatment to a work injury; because it was not preceded by an initial utilization review, where applicable; inconsistency between the provider and the treatment to be reviewed and/or lack of specificity concerning treatment dates.

within thirty days of their submission to the insurance company. 77 P.S § 531(5). Otherwise, this obligation can only be extinguished by an order of a workers' compensation judge or the consent of the injured worker. If an employer or insurer takes a supersedeas which has not been authorized by proper invocation of utilization review, it is subject to penalties pursuant to Section 435 of the Act, 77 P.S. § 991. The Bureau's Compliance Division is also authorized to take action against the non-paying employer. Finally, the employer's obligation to pay can be enforced by a medical provider through a Petition for Fee Review, which can result in an order to pay and the imposition of an interest award against the insurer or employer.

Upon approval of a request for utilization review, the Bureau assigns the case to a URO and provides notice of the assignment to the injured worker, the insurer, the employer and the medical provider under review, with instructions to the URO and the medical provider. Prior to the Third Circuit's decision in this case, there was no notice to injured workers that their medical benefits might be stopped. In the usual case, the workers would learn from the medical providers that benefits had been stopped, and, in most cases, that treatment would no longer be provided.

Once the URO receives the assignment, it is required to render a decision within sixty days of the assignment as to whether the challenged treatment is reasonable and necessary. 77 P.S. § 531(6)(ii).[15] Prior to the Third Circuit's decision, the injured worker was precluded from any participation in the utilization review, either directly or through counsel. The URO was instructed by the Bureau not to discuss the treatment under review with the injured worker or his or her attorney, and could not accept documents or other evidence from the injured worker. The URO is statutorily directed to

[15] The statute does not dictate how long the Commonwealth has to make the assignment. Thus, the initial review may be delayed well beyond the sixty days provided in the statute, as some of the named plaintiffs have alleged, *See* Jnt. App. at 39, ¶ 231 (assignment took 32 days); ¶250-1(42 days).

file a copy of its report with the Bureau, which monitors and supervises the performance of the URO's.[16]

District Court Proceedings

On January 12, 1995, Plaintiffs filed their initial complaint challenging the supersedeas provisions contained in Section 306(f.1)(5).[17] They claimed that those provisions

[16] Petitioners deny that medical benefits are at issue at all, characterizing the dispute as one over "bills", rather than treatment, and by insisting that the Plaintiffs can be fully reimbursed later for any loss they incur now. This mischaracterizes the nature of the benefit delivery system at issue here, which provides benefits to injured workers through the receipt of treatment, and not by way of direct payments to injured workers. In practice, those benefits are furnished through the payment of medical bills submitted by medical providers to the insurance company or employer. Thus, while it may be true in some sense that "bills" are at issue here, those bills are merely the vehicle through which medical benefits are provided under the Act. When the bills are not paid, Plaintiffs' treatment is ordinarily stopped, and benefits are thereby eliminated. The consequences of this can be severe and permanent. This is particularly true where the length of the deprivation is prolonged, as the Plaintiffs have alleged here. Moreover, it is simply not true that the dispute centers around treatment which has already been delivered. In some cases, where a discrete procedure is involved, this may be the case, but in most cases, like those of the named Plaintiffs, the utilization review was used to supersede not only payment for past treatment, but for ongoing treatment as well. As the named Plaintiffs have alleged, such treatment will not be restored until after the utilization review has been completed, including, if the initial review is adverse to the injured worker, appeals to the workers' compensation system.

[17] Petitioners object to the term "supersedeas" because that term does not appear in the statute. Plaintiffs have used the term throughout this litigation because the challenged provisions permit employers to supersede, or stop, their medical treatment. Even the Director of the Bureau has referred to it as an "automatic supersedeas". *See* Appendix to Plaintiff's Motion for Partial Summary Judgment, Exhibit "F" at 11. Plaintiffs continue to use the term supersedeas because it is most descriptive of what the statute provides. To supersede is to "set aside, render unnecessary, suspend or stay". BLACK'S LAW DICTIONARY, 4th Ed. (1951).

violated their right to due process of law, because they provided for the cessation of workers' compensation medical benefits pending "utilization review" with no pre-deprivation notice or opportunity to be heard.

The originally named Plaintiffs included seven seriously injured workers whose benefits had been stopped under the supersedeas procedure of 306(f.1)(5), and the Philadelphia Area Project on Occupational Safety and Health (Phila-POSH). They initiated, on behalf of themselves and a class of similarly situated injured workers, a facial challenge to the constitutionality of Sections 306(f.1)(5) and (6) of the Act.

The named defendants included the Commonwealth through four state officials responsible for designing, implementing, administering and enforcing the Act, the director of the legislatively created State Workers' Insurance Fund (SWIF), the School District of Philadelphia, which is a self-insured public employer, and seven of the ten insurance carriers who are Petitioners herein, licensed to write workers' compensation insurance policies in Pennsylvania. On March 30, 1995, the Philadelphia Federation of Teachers was permitted to intervene as an additional plaintiff.

On April 10, 1995 the insurers moved under Federal Rule of Civil Procedure 12(b)(6) to dismiss the complaint as to them, alleging that they were not state actors for purposes of the Fourteenth Amendment. On January 24, 1996, the district court entered an order granting the defendant insurance companies' motion to dismiss.

On May 29, 1996, Respondents filed an Amended Complaint which added three additional plaintiffs (also Respondents herein) and additional constitutional claims.[18] The

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[18] The Amended Complaint extended Plaintiffs' challenge to include the utilization review provisions which are contained in Section 306(f.1)(6). Plaintiffs also made a due process attack upon the fees imposed in the reconsideration review process, and the lack of standards to govern utilization review and appeals therefrom. The Third Circuit ruled against the Plaintiffs on the latter claim, but remanded for further proceedings on the reconsideration issue. This claim was a systemic one

insurers were served with the Amended Complaint, and at the same time dismissed from the case in light of the court's prior state action decision. On June 19, 1996, the Commonwealth defendants filed a motion to dismiss the Amended Complaint. By order dated November 8, 1996, the court dismissed the Commonwealth defendants, finding that Sections 306(f.1)(5) and (6) caused a deprivation of a property interest, but that the provisions were nonetheless constitutional. This left the School District as the sole remaining defendant. The School District filed a Motion for Judgment on the Pleadings based upon the court's finding of constitutionality. This motion was granted on December 16, 1996. This constituted a final order, from which Respondents appealed to the United States Court of Appeals for the Third Circuit.

The Appellate Proceedings

On March 13, 1998, the United States Court of Appeals for the Third Circuit reversed the decisions of the district court and held that the supersedeas provisions of the Act violated the requisites of procedural due process. Citing to the well-worn precedents of this Court, the Third Circuit held that both the lack of adequate pre-deprivation notice and the denial of an injured worker's right to be heard rendered the supersedeas provisions constitutionally infirm.[19]

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which ran against the Commonwealth defendants. It was settled on August 19, 1998 at a meeting of all counsel to the proceedings below. Plaintiffs cannot fathom, therefore, why it is addressed in the School District's brief. It was not raised in any of the Petitions for Certiorari, including the School District's, which was denied by the Court, and is clearly not before the Court for disposition.

[19] "[W]e hold that the supersedeas provisions under § 531(5) and (6) violate the dictates of due process by not affording disabled employees notice or an opportunity to be heard before their medical benefits are suspended. To remedy the procedural defects in the statute, at minimum, an employee must be given: (1) timely and reasonable notice of the imminent suspension of the medical benefits and treatment before the suspension takes effect; (2) a description of the reasons why utilization review has been invoked; (3) an opportunity and time to submit a personal statement in writing regarding the employee's view of the reasonableness and/or

More important to the issues presented here, the Third Circuit held that the insurers were state actors when they invoked the unconstitutional supersedeas provisions in the Act. Relying on *Edmonson v. Leesville Concrete Co.*, 500 U.S. 614 (1991)and *Tulsa v. Professional Collection Services, Inc. v. Pope*, 485 U.S. 478 (1988), the court found that the decision to invoke utilization review was not self-executing, but rather, required the overt assistance of the Bureau. The court held that," [t]he [Bureau] is intimately involved throughout, and without that involvement the supersedeas could not operate." Pet. App. at 15a.

I. INTRODUCTION AND SUMMARY OF ARGUMENT

The Plaintiffs in this case have directly challenged the constitutionality of § 306(f.1)(5) and (6) of the Pennsylvania Workers' Compensation Act, which delegates to employers the power to stop the medical benefits of injured Pennsylvania workers. Because Plaintiffs are making a facial challenge to the constitutionality of the utilization review procedures in the Pennsylvania Act, (a challenge directed equally against the Commonwealth Defendants and the Petitioners), this case falls squarely within a well established line of Supreme Court precedents that have found state action on the part of a private actor or entity without applying the discrete state action "tests" relied upon by Petitioners. *Tulsa, supra*; *Reitman v. Mulkey*, 387 U.S. 369 (1967); *Smith v. Allwright*, 321 U.S. 649 (1944); *Nixon v. Condon*, 286 U.S. 73 (1932); *Accord New York Times Co. v. Sullivan*, 376 U.S. 254 (1964). In these cases, the challenge to the constitutionality of the state law by necessity places the focus on the state statute and its underlying policy, regardless of the identity of the defendant, and requires the court to analyze within the context of the overall statutory scheme, any act or decision by a private actor or entity who is relying on the challenged law. *See, e.g., Tulsa,*

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necessity of the disputed medical treatments; and (4) a description of the procedures under which the employee can appeal an adverse determination." Pet. App. at 33a.

485 U.S. at 480. In applying this contextual approach to the state action issue, this Court has relied upon the totality of the circumstances, and framed the issue in terms of whether, after passage of a given act, the state's involvement with the statute (as opposed to that of the private actor or entity) is substantial enough to implicate the protections of the Constitution. *Tulsa*, 485 U.S. at 486.

When a facial challenge is made to the constitutionality of a state law, the first question the Court must address is not whether the private actor or entity invoking the law is a state actor, but rather, whether the challenged provisions of the law are constitutional. *See, e.g., Tulsa, supra*. Significantly, when the Court has used this approach, and found that the law violates the procedural due process or the equal protection clause, it has invariably found that the private actor or entity invoking or relying on the unconstitutional law is a state actor. *Tulsa, supra*; *Fuentes v. Shevin*, 407 U.S. 67 (1972); *Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969); *Reitman v. Mulkey, supra; Smith v. Allwright, supra*; *Nixon v. Condon, supra*; *Accord New York Times, Co. v. Sullivan, supra*.[20]

Pursuant to the above cited line of cases, the Petitioners' reliance on the unconstitutional provisions of the Pennsylvania statute to stop Plaintiffs' entitlement to medical treatment was clearly state action. In invoking the unconstitutional provisions of the Pennsylvania Act, which delegated to employers the power to terminate a vested state entitlement, Petitioners were not only exercising a state granted power, but also, promoting the state's policy of cost containment. The purpose and effect of the 1993 Amendments to the Pennsylvania Workers Compensation Act was therefore to enlist or "harness the energies of private groups to do indirectly what

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[20] In cases such as *Fuentes* and *Sniadach* the Court did not even feel the need to address the state action question, as the facial attack apparently rendered that unnecessary. *See generally* Brest, "State Action and Liberal Theory: A Casenote on *Flagg Brothers v. Brooks*", 130 Pa. L.Rev. 1296 (1982).

[the state] could not [constitutionally] . . . do [itself]". *Reitman*, 387 U.S. at 383 (Douglas, J., concurring); *Cf. Lebron v. National Railroad Passenger Corp.*, 513 U.S. 374, 397 (1995) ("It surely cannot be that government, state or federal, is able to evade the most solemn obligations imposed in the Constitution by simply resorting to the corporate form."). In promoting the state's policy, Petitioners represented the state and became its agent. *Nixon*, 286 U.S. at 89. As the above cited line of cases teaches, "the government's reliance on the willing compliance of private citizens is a factor increasing – not diminishing – the government's involvement," thereby rendering the private citizen, whose energies were harnessed by the express authorization of the statute, a state actor. *Alliance For Community Media v. F.C.C.*, 10 F.3d 812, 822 n.13 (D.C. Cir. 1993), *aff'd in part, reversed in part*, 516 U.S. 973 (1995).

In stark contrast to the cases involving a direct challenge to the constitutionality of a state statute are those primarily relied upon by Petitioners, which, because they did not involve a direct constitutional challenge, steer the court's focus away from the state and on to the conduct or decision of the private actor or entity.[21] Because in these cases the law or regulation relied on by the private actor or entity was not directly challenged as unconstitutional, the state was not directly implicated in the private act or decision. Thus, in order to determine whether the private conduct or act could be deemed "fairly attributable to the state", the court had to rely on certain guiding principles. *Edmonson, supra*, 500 U.S. at 621-23. While it is Plaintiffs' position that their facial challenge to the constitutionality of the Pennsylvania Act renders these guiding principles and the decisions that established and utilized them inapplicable to this case, even assuming that they do apply, Plaintiffs contend that the Petitioners both misstated and misapplied the appropriate principles, and that

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[21] *See eg. Rendell-Baker v. Kohn*, 457 U.S. 830 (1982); *Blum v. Yaretsky*, 457 U.S. 991 (1982); *Flagg Brothers , Inc. v. Brooks*, 436 U.S. 149 (1978); *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345 (1974).

the Third Circuit's approach was consistent with this Court's most recent state action cases. Indeed, Petitioners' rigid approach completely ignores the evolution of the doctrine set forth in this Court's most recent state action pronouncements. *Id.; West v. Atkins*, 487 U.S. 42 (1988). Contrary to this Court's flexible, contextual approach to discerning state action, Petitioners argue for the strict application of discrete tests (public function, symbiotic relationship, state compulsion), and would require satisfaction of those tests individually before state action could be found.

On numerous occasions this Court has stated that the so-called "tests" espoused by Petitioners are in reality only factors or guiding principles to be considered in the overall analysis as to whether, given all the facts and circumstances of the particular context, state action can be said to exist. Plaintiffs contend that this totality approach is the appropriate one for the Court to continue to employ and that, under it, the insurers are clearly state actors when invoking the utilization review process. In addition, Plaintiffs also contend that even under the more restrictive approach that Petitioners have asked this Court to adopt, the insurers' role in the utilization review process renders them state actors.

II. THE THIRD CIRCUIT CORRECTLY HELD THAT THE UTILIZATION REVIEW PROVISIONS VIOLATED DUE PROCESS

While it is the Plaintiffs' contention that the due process issue is not appropriately before this Court, the Third Circuit's due process decision was based on this Court's well established precedent and is virtually unassailable. The court held that the utilization review provisions violated due process because the statute provided no notice to Plaintiffs prior to the supersedeas of their medical benefits, and offered the injured workers no opportunity to challenge the suspension of their medical benefits until many months (at least) after the deprivation of those benefits had been effected. The court found the lack of pre-deprivation notice to the injured worker

to be constitutionally fatal.[22] Moreover, the court observed, the notice arrived after the benefits had already been stopped. The court noted the Commonwealth's concession that no notice is afforded to the injured worker under the statute, and concluded that inadequate notice effectively strips an injured worker of his ability or opportunity to protest or minimize unjustified deprivations. The court held that due process requires some sort of opportunity to be heard regarding the basis of the proposed termination before it takes place.

The Third Circuit's holding is a mainstream decision consistent with a well-settled and unbroken line of precedent from this Court, which sets forth two basic tenets of due process. First, "notice reasonably calculated under all the circumstances to apprise interested parties of the pendency of the action" is constitutionally required prior to the deprivation of a protected property interest. *Memphis Light, Gas & Water Div. v. Craft*, 436 U.S. 1, 13 (1978); Second, due process ordinarily requires an opportunity for "some kind of hearing" prior to the deprivation of such an interest. *Memphis Light, Gas & Water, supra*, 436 U.S at 19, *citing, Boddie v. Connecticut*, 401 U.S. 371, 379 (1971). *See also Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 437 (1982). In a case such as this, in which an established state procedure is being challenged, this Court has always required notice and an opportunity to be heard *before* the deprivation, unless exigent circumstances exist or pre-deprivation process would be demonstrably impracticable. *Zinermon v. Burch*, 494 U.S. 113 (1990); *Parratt v. Taylor*, 451 U.S. 527 (1981). This is true even if extensive post-deprivation remedies are afforded. *Connecticut v. Doehr*, 501 U.S. 1 (1991).

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[22] The Third Circuit found the notice constitutionally defective in many respects: "[It] does not explain that a supersedeas or suspension of one's medical benefits may result nor does it explain what utilization review entails. In addition, it does not inform an employee of any procedures under which the employee can protest the suspension of the medical benefits or contest the merits on which the proposed deprivation is based." Pet. App.at 23a.

This Court has applied these principles in numerous factual contexts to invalidate state laws that failed to provide any notice or opportunity to be heard before the deprivation of a protected liberty or property interest.[23] These cases and the due process principles enunciated in them apply to interim deprivations of property as well as to final deprivations. *See, e.g., Connecticut v. Doehr*, 501 U.S. at 12; *Arizona v. California*, 460 U.S. 605, 638 n.28 (1983).

Because no one disputes that the challenged statute permitted a recognized property right to be disrupted without any pre-deprivation notice, the Third Circuit's decision that the statute was unconstitutional must stand regardless of how this Court might view the other due process concerns raised by Petitioners. Inadequate notice is enough by itself to render the statute unconstitutional and is enough to support the Third Circuit's due process holding. *See, e.g., Memphis Light, supra; Mullane v. Central Hanover Bank and Trust Co.*, 339 U.S. 306, 314 (1950).

The Third Circuit's determination that the lack of a prior opportunity to be heard renders the statute unconstitutional also must be upheld. Once it is established that pre-deprivation process is due, *Mathews, supra*, defines the extensiveness of the procedures to be afforded. The Third Circuit straightforwardly applied the three *Mathews* factors and concluded that the injured workers must be afforded an opportunity to submit a personal statement in writing to the utilization reviewer before his benefits can be stopped. The Court looked first at the private interests involved, including the injured workers' interest in the relief that medical treatment provides, and the interest of the insurers and employers in not paying for unnecessary and unreasonable medical treatment. While

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[23] *Connecticut v. Doehr, supra* (real estate attachment); *Cleveland Board of Education v. Loudermill*, 470 U.S. 532 (1985) (public employment); *Logan v. Zimmerman Brush, supra* (cause of action); *Memphis Light, Gas & Water Division, supra* (utilities); *Goss v. Lopez*, 419 U.S. 565 (1975) (public education); *Fuentes v. Shevin*, 407 U.S. 67 (1972) (personal property); *Bell v. Burson*, 402 U.S. 535 (1971) (drivers licenses); *Goldberg v. Kelly*, 397 U.S. 254 (1970) (welfare benefits)

the employers' interest was pecuniary, the injured workers' was not. Their interest was considered by the Court to be significant.[24] The Court further concluded that the risk of erroneous deprivation was unacceptably high, given the injured workers' lack of notice and opportunity to be heard during the utilization review process. Although the review focuses upon the medical records of the treating physician, and the physician must be given the chance to speak with the reviewer, the court was "hard-pressed to believe that the portrait of the employee's illness and treatment . . . [could be] . . . complete without a statement or other input from the injured worker". Pet. App. at 29a. The governmental interest, according to the court, would also be served by permitting the injured worker a pre-termination opportunity to respond. The government has a legitimate interest in containing costs and ensuring that benefits are paid only for reasonable and necessary treatment, but has an equally compelling interest in preventing the erroneous termination of benefits to injured workers who have a continuing need for them. On balance, therefore, some sort of pre-deprivation process would be

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[24] The Petitioner-Insurer's assertion that the Third Circuit failed to take their interest into account was erroneous. The court factored their interest into the *Mathews* analysis but concluded that it was not as significant as the injured workers' in light of the purposes and policies of the Act. While the insurers' interest could be quantified in monetary terms, timely medical treatment only has value at the time it is needed, and the consequences of delay in this context can lead to medical consequences which can never be rectified through the retroactive payment of money. Pet. App. at 28a; *See also Memorial Hospital v. Maricopa County*, 415 U.S. 250, 259-261 (1974). It should be noted that the Pennsylvania courts have balanced the interests of employers and injured workers and come to the same conclusion as the Third Circuit did. *Stonebraker v. Workers' Compensation Appeal Board*, 163 Pa.Cmwlth. 468, 475 (1994) (despite employer's economic interest in terminating medical treatment which is not necessary as soon as possible, injured workers should be protected from potentially devastating economic or medical consequences stemming from unwarranted terminations of medical benefits).

necessary. Pet. App. at 30a. At a minimum, the Court concluded, "the employee should be granted the opportunity to present additional evidence such as his/her personal testimony in writing as to the reasonableness and necessity of the disputed treatment". Pet. App. at 31a.

The Third Circuit's holding was well within the parameters set forth in *Mathews*. Indeed, the plaintiff in *Mathews* received far more in the way of pre-deprivation process than did the *Sullivan* plaintiffs. Moreover, the Petitioners have alleged no exigency which would justify a departure from the fundamental requirements of pre-deprivation process. Neither is impracticability a barrier, as demonstrated by the existence of a system for the predeprivation review of medical benefits prior to the adoption of the utilization review provisions at issue here, and the implementation of prior notice and opportunity to be heard by the Commonwealth defendants following the Third Circuit's decision. Even in those rare situations in which this Court has approved post-deprivation procedures alone, it has required some assurance against arbitrary and unfounded interference in the enjoyment of the property interest. *E.g., Connecticut v. Doehr, supra*. Here, there is no such assurance. The employer's request for utilization review is not required to be based on any medical criteria whatsoever, or supported by even the slightest indicia of reasonableness. This Court has found on numerous occasions that "one-sided, self-serving, and conclusory submissions" elevate the risk of erroneous deprivation to an unacceptable level. *Id., Fuentes v. Shevin, supra*, 407 U.S. at 83.

Underlying the Petitioners' argument is the fundamental complaint that due process was found to attach at all, because what is at issue here, in their view, is not the deprivation of medical benefits, but the timing of payment for treatment already received. Bills, not benefits, is how the Petitioners would like to characterize what is at stake here. Petitioners' argument grossly mischaracterizes the record and the clear import of a request for utilization review. Medical bills are the vehicle through which medical benefits are delivered to injured workers in Pennsylvania. These benefits are public

benefits and the state has exclusive control over the resolution of disputes among the parties in the administration of those benefits. The procedures so utilized must satisfy due process. *Logan v. Zimmerman Brush*, 455 U.S. at 429 n.5. Unless the doctor or other medical provider agrees to work for free, once payments stop, so does the treatment. Several of the Plaintiffs in this action have alleged that their ongoing medical treatment was stopped once the insurer or employer stopped paying for it on the basis of a utilization review request. They are precluded by law from paying for those services themselves in the interim, and thus, unlike the Plaintiff in *Mathews*, have no access to substitute services while they await the outcome of utilization review.[25]

III. PLAINTIFFS' FACIAL CHALLENGE RENDERS THE DISCRETE TESTS INAPPLICABLE AND DIRECTLY IMPLICATES THE STATE IN THE DECISION TO STOP MEDICAL BENEFITS.

It is a basic proposition that a State acts through its legislative, its executive and its judicial branches. *Ex Parte Virginia*, 100 U.S. 339, 347 (1879). The enactment of a state law and its enforcement is undisputably state action. *Tulsa*, 485 U.S. at 486-87; *New York Times*, 376 U.S. at 265; *Paul v. Watchtower Bible and Tract Society*, 819 F.2d 875, 880 (9th Cir. 1987); Strickland, *The State Action Doctrine and the Rehnquist Court*, 18 Hastings Const. L. Q. 587, 598, 601-602 (1991). When a facial challenge is made to the constitutionality of a state law and its enforcement in a particular

[25] None of the Petitioners ever challenged the accuracy of this fact in the proceedings below, nor could they, given the explicitness of the law on this point. The fact that one of the named Plaintiffs was forced by a medical provider to pay for her treatment during utilization review does not change the fact that it was illegal for the doctor to demand payment from her. David Weyl, Chief of the Bureau's Cost Containment Division testified emphatically on this point: "If that provider accepts money from the claimant, that provider has violated the law. The workers' compensation law absolutely prohibits taking money from claimants for any medical treatment that is provided under the Act, period." Third Cir. App. at B-155.

case, this Court has consistently held that the enactment and enforcement of an unconstitutional state law is state action. *BMW of North America, Inc. v. Gore*, 517 U.S. 559, 573 n.17 (1996); *Tulsa*, 485 U.S. at 488; *Cohen v. Cowles Media Co.*, 501 U.S. 663, 668 (1991); *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886, 916 (1982); *New York Times*, 376 U.S. at 265; Krotoszynski, *Back to the Briar Patch: An Argument In Favor Of Constitutional Meta-Analysis in State Action Determinations*, 94 Mich. L. Rev. 302, 315 (1994); Strickland, *supra*, 18 Hastings Const. L. Q. at 606.

Under these circumstances, and without using the discrete state action "tests" relied upon by Petitioners, this Court has imposed liability on private persons who either invoke the unconstitutional law to deprive a person of a constitutional right, *See, e.g., New York Times, supra*, or rely on authority granted by the unconstitutional law to deprive a person of a constitutional right. *See, e.g., Tulsa, supra*. In the *New York Times* line of cases, the enforcement of the unconstitutional law occurs in the context of a judicial proceeding, whereas in cases such as *Nixon, Reitman* and *Tulsa* the enforcement of the unconstitutional law is accomplished by a private person or entity pursuant to the terms or authorization of a state statute or state constitutional amendment. When a court enforces an unconstitutional law there is clearly state action, and the private party invoking the unconstitutional law is liable. *New York Times, supra*. On the other hand, when the enforcement of the unconstitutional law is accomplished by a private person or entity pursuant to the terms or authorization of a state law this Court has relied on two distinct but related rationales, neither of which requires application of the discrete "tests", to find private entities liable when invoking the unconstitutional law. Pursuant to *Tulsa*, the private person relying on the unconstitutional law is liable if, after the passage of the act, the state's involvement with the statute is substantial enough to implicate the protections of the Constitution. *Tulsa*, 485 U.S. at 486. This occurs, and state action is present, "when private parties make use of state procedures with the overt and significant assistance of state officials." *Id.* In cases such as *Nixon* and *Reitman*, the Court looked to

whether the state has delegated a state power or function to a private entity or authorized a private entity to do indirectly what the state could not do directly. Instead of applying discrete tests, the Court focuses on the purpose and impact of the state law and holds the private actor accountable for carrying out the state's unconstitutional policy.

The Court's decision in *Tulsa* directly controls this case. That analysis, which would view Petitioners' decision to invoke utilization review and stop medical benefits in the context of the overall statutory scheme, makes it clear that after passage of the Act the state's involvement with the statute was substantial, and that in invoking the unconstitutional provisions of the Act, Petitioners are liable for the violation of Plaintiffs' right to procedural due process.

Pennsylvania's involvement with the statutory process of utilization review is not only extensive, but also much more substantial than the state's involvement with the non-claim statute at issue in *Tulsa*. Like the non-claim statute involved in *Tulsa*, under the Pennsylvania Act the employer's request for utilization review is not self-executing. In order to invoke the statutorily created and state-administrated process of utilization review, and hence to exercise the state authorized power to stop a state entitlement, the employer must first initiate a legal process. This is done by filing a Request for Utilization Review on a form provided by the state with the Pennsylvania Bureau of Workers' Compensation, which is a state agency. Under the Act, while the decision to invoke the statutory process is placed in the hands of the employer, the decision to grant utilization review is retained by the state. If a request is improper or the form is incorrectly filed, the state rejects it and the employer's statutory obligation to provide medical benefits continues. Accordingly, without the overt assistance of the state, the employers have no authority under the Act to stop the medical benefit.

In addition to this overt and significant involvement on the part of state officials in the initiation of utilization review,

the statute directly involves the state, on a day by day basis, in the implementation of the workers' compensation benefit program, and in the enforcement of the employer's decision to seek utilization review. Unlike a private contractual arrangement, absent the state's express authorization, the employers do not have the power or right to deny payment for medical bills that they deem unnecessary or unreasonable. Contrary to the Petitioners' implication that the nonpayment of disputed bills is an accepted business practice, under the Act they are not operating in a private business sphere, but are delivering public benefits which are constitutionally protected from arbitrary deprivations. Accordingly, if the employer fails to file for utilization review or is denied utilization review by the Bureau and attempts to avoid payment of a medical bill that the employer deems unreasonable, the statute authorizes the Bureau's Compliance Division to step in and impose sanctions on the employer. Pursuant to the commands of the statute, the state is therefore involved in policing the employers and in taking aggressive steps to ensure compliance with the Act's terms.

More significantly, an employer's decision to invoke utilization review does not exist in a vacuum, but rather, requires the state's involvement for both approval and enforcement of the decision. The decision to invoke utilization review and to supersede the injured workers' medical benefits is only the first step in what invariably turns out to be a lengthy legal process – a process that is dictated by the state statute, involves the use of state established procedures, state offices and hearing rooms, and state employees at every step of the proceedings.

First, as mentioned above, the initial request for utilization review relies on state forms and requires approval by the Bureau, a state agency staffed by state employees. Employers have no access to the URO outside of this state-created structure. Second, under the statute, in order for the employers to maintain their supersedeas of the injured workers' medical benefits, they must have access to utilization review, which can only be gained through Bureau permission. The state, through the Bureau, is involved in the

approval, training and supervising of the URO's. In addition, the decision on the reasonableness and necessity of the medical treatment in question must be rendered in accordance with the statute, which requires a written report within sixty days of assignment to the URO. The state both supervises and monitors the URO's to ensure compliance with the statute. The state therefore plays an active role by setting standards for the URO's, providing them guidance, and monitoring them to ensure compliance with the statutory requirements. The active role played by the state in relation to the URO's and their decision making process directly involves the state in the utilization review process.

Third, under the Act, the URO's decision can be appealed to a workers' compensation judge, where the injured worker is entitled to a hearing, the right to testify on his behalf, the right to be represented by counsel, and the right to present medical evidence and cross examine the employer's medical expert. The workers' compensation judge is a state employee and the hearing takes place in state facilities. When the proceedings reach this stage, the decision by an employer to invoke utilization review directly involves the state. If the workers' compensation judge rules in favor of the injured worker, it is the state that will revoke the employer's decision to terminate the treatment. If the workers' compensation judge upholds the employer's initial determination to stop the medical benefits, it is the state that will place its imprimatur on that decision, a decision that will have been reached without providing the injured worker any pretermination notice or opportunity to be heard.

The employers' power to stop benefits to injured workers therefore emanates from the state and is dependent upon the state's approval at every key juncture. Without the "overt, significant assistance of state officials", employers would not be able to initiate or sustain the deprivation challenged in this case. *Tulsa*, 485 U.S. at 487.

While *Tulsa* controls this case, Petitioners are also liable for violation of the injured workers' right to procedural due process pursuant to a line of cases that has held that a state may not avoid the strictures of the Constitution by delegating

to private persons or entities the power or authority to do indirectly what the state cannot do directly.[26] *See, e.g., Reitman, supra* at 380-381; *Cf. Lebron*, 513 U.S. at 397. In these circumstances, when the state delegates to private persons or entities a governmental power or function, and the private entity exercises that governmental power or function in a manner that violates a constitutionally protected right, this Court has consistently held that the private person or entity who exercises the governmental power is a state actor. *West*, 487 U.S. at 54; *Evans v. Newton*, 382 U.S. 296, 299 (1966) ("When private individuals or groups are endowed by the state with powers or functions governmental in nature, they become agencies or instrumentalities of the State and subject to its constitutional limitations.").

Two controlling principles emerge from these cases. First, in all of the above cited cases, the authority exercised by the private actor or entity was derived directly from a state statute or constitutional amendment. Without this delegation from the state, the private actor or entity would be powerless to act in the manner prescribed by the statute or state constitutional amendment. *See, e.g., Nixon*, 286 U.S. at 85; *Reitman*, 387 U.S. at 379. The power exercised by the private actor or entity is therefore state power.

Second, in most of the cases, there was at least some indication that by delegating to private actors or entities a

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[26] These cases serve an important purpose in the state action inquiry. Pursuant to the Court's decision in *Tulsa*, state action existed because the state played an overt role in the administration of the statute. However, a state could avoid liability under *Tulsa* by enacting a statute that ceded all state power to the private entity, and in which the state played no role other than enacting the statute. This problem was identified by Justice Stevens dissenting in *Flagg Brothers*, 436 U.S. at 175. In these circumstances, if the state has delegated a state power or function to a private individual or entity in an attempt to avoid the strictures of the Constitution, the above line of cases would still hold the private actor or entity accountable for exercising a state power or function in a manner that violated the Constitution. This prevents the state from doing indirectly what it constitutionally cannot do directly.

state power or function, the state was attempting to evade the strictures of the Constitution, or do indirectly what it constitutionally could not do directly. For example in *Reitman*, the Court placed great weight on the fact that the state supreme court had construed the state constitutional amendment, which was neutral on its face, as authorizing private racial discrimination. *Id.* at 375-76. The state had delegated a power that allowed private individuals to discriminate based on race, something the state could not have done directly. The Court in *Reitman* also noted that, in construing the state amendment to determine whether the delegation was an attempt to evade the strictures of the Constitution, the state court correctly analyzed the law in terms of (1) its immediate objective, (2) the context in which the delegation arose, and (3) the ultimate effect or impact of the delegation. *Id.*; *See also Alliance for Community Media v. F.C.C.*, 10 F.3d at 820.

Applying these principles to the 1993 Amendments, it is clear that Pennsylvania was attempting to evade the strictures of the due process clause by delegating to employers the power to stop or supersede medical benefits without providing pre-deprivation notice or an opportunity to be heard. First, prior to the 1993 Amendments, medical benefits could only be superseded by a state workers' compensation judge after the injured worker had been provided notice and a hearing on the necessity and reasonableness of the treatment. The Amendments delegated to the employers both the state power to initially determine whether the treatment was reasonable and necessary and to stop treatment on that basis.

Second, the state's purpose in delegating this power to the employers was clearly to evade the strictures of the due process clause. The record establishes that the 1993 Amendments were part of a cost containment package ostensibly enacted in order to reduce workers' compensation insurance and thereby attract more business to Pennsylvania. However, in enacting these provisions, the state was aware that it could not directly terminate medical benefits without providing notice or an opportunity to be heard. The 1993 Amendments were not passed in a legal vacuum. Prior to their enactment, almost identical provisions in the Pennsylvania Workers'

Compensation Act had been struck down as unconstitutional. *Baksalary, supra*. It is clear that the state was attempting to harness the energy of the private insurers to carry out the state policy of cost containment and to do indirectly what the state could not constitutionally do directly. The delegation to the employers of the state power to stop or supersede a state entitlement not only violated the state's constitutional duty to provide adequate procedural safeguards, *Logan, supra,* but also made the employers state actors when invoking the unconstitutional procedures. *West, supra*; *Evans, supra*; *Reitman, supra*; *Nixon, supra*. The delegation of the state power of supersedeas to the employers makes this case even more compelling than *Tulsa*. Here, not only was the state substantially involved in the utilization review process, but also, in establishing the utilization review process it was clearly trying to evade "the most solemn obligations imposed" by the due process clause. Pursuant to this Court's decision in *Tulsa* and the above cited delegation cases, Petitioners are clearly state actors.

A. A TOTALITY OF THE CIRCUMSTANCES APPROACH SHOULD BE USED TO FIND STATE ACTION WHERE THERE IS NO FACIAL CONSTITUTIONAL CHALLENGE

1. *Edmonson's* Totality Test

Edmonson was this Court's last major foray into the realm of state action in a case that did not involve a facial challenge to the constitutionality of a state law. The Court's analysis in that case is contrary to the Petitioners' contention that state action can only be established through the rigid application of formulaic rules. Rather, the Court embarked upon a unified state action analysis which took into account 1) the extent to which the actor relies on governmental assistance and benefits; 2) whether the actor is performing a traditional governmental function; and 3) whether the injury caused is aggravated in a unique way by the incidents of governmental authority. *Edmonson*, 500 U.S. at 621-22.

Instead of stating a series of discrete tests and applying them separately to determine whether each by itself was satisfied, the Court considered the facts relevant to these principles and weighed them to determine whether, all things considered, the otherwise private actor fairly could be deemed a state actor. Essentially, the Court adopted a "totality of the circumstances" test.

The approach used by the Court in *Edmonson* is particularly appropriate to discern state action, which in any given circumstance is necessarily a "fact-bound inquiry." For, as this Court has indicated on numerous occasions, "only by sifting facts and weighing circumstances can the non-obvious involvement of the State in private conduct be attributed its true significance". *Lugar v. Edmondson Oil Co*, 457 U.S. 922, 939 (1982). The totality approach relied upon by the Court in *Edmonson* was not a unique or radical departure from the analysis applied in previous state action cases, and was consistent with a number of other decisions in which the Court utilized no specific litmus test, but rather, considered all the facts and circumstances to determine whether the challenged action could be fairly attributed to the state. *See, e.g., West*, 487 U.S. at 55-56; *Tulsa*, 485 U.S. at 479; *see also Burton*, 365 U.S. at 725-26.

The approach used by the Court in *Edmonson*, *West*, and *Tulsa*, its most recent state action cases, is undoubtedly the most reliable method of analysis for discerning state action. The Court has consistently recognized the complexity of the state action inquiry and the factual subtleties which necessarily bear upon the analysis. There is no discrete test which can neatly categorize purportedly private decisions into state action or non-state action pigeonholes. The Petitioners' plea for the adoption of such a test to resolve the "most troublesome issue in constitutional law"[27] is overly simplistic and inconsistent with this Court's most recent pronouncements. It should be rejected. In determining when private conduct can

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[27] Strickland, 18 Hastings Const. L.Q., *supra*, at 588.

be deemed fairly attributable to the state, each situation must be factually analyzed on its own terms.

2. Application of the Totality Test To The Employer's Role in Utilization Review

Application of the *Edmonson* totality approach to the utilization review process at issue here demonstrates that the Third Circuit correctly deemed the employers to be state actors. As this Court has instructed, those procedures and the employers' role in that process must first be viewed in the context of the workers' compensation system as a whole, with its dense web of interconnections between the state agency and the employers who fulfill the state's obligation to Pennsylvania's injured workers. *See* Pet. App. at 25a. *See also West*, 487 U.S. at 56 ("Whether a physician is on the state payroll or is paid by contract, the dispositive issue concerns the relationship among the State, the physician, and the prisoner."). The interconnections between the state and the employers are so numerous and so strong, that a finding of state action is clearly warranted.

a. Governmental Assistance and Benefits

The extent to which the employers rely upon "governmental assistance and benefits" weighs heavily in this case in favor of a finding of state action. The utilization review process is a discrete aspect of the workers' compensation program, one which is established by state law and administered directly by the state for the purpose of delivering public benefits to injured workers without regard to fault. The state acts as a giant funnel through which almost every transaction in the system must pass. The state chooses who the system's participants will be and defines the roles that each will play within the system. The state controls all entrances into and exits from the system and supplies all the rules, regulations, forms, physical offices, hearing rooms, and decision makers. It resolves all disputes as to injured worker eligibility and employer obligations. It is a "system which the government alone administers." *Edmonson*, 500 U.S. at 622.

As in every other context in the Pennsylvania system in which an employer wishes to change the status quo without an injured worker's consent, an employer seeking utilization review must initiate a legal process exclusively administered by the state. Any effort to take a "self-executing" supersedeas, one which is not premised upon a properly submitted request for utilization review, violates the Act and is subject to penalties by the Bureau. Aside from utilization review and the supersedeas of benefits that it permits, and absent consent by an injured worker, a stoppage of medical benefits can only be effectuated by the direct action of state officials. The request for review is only the first step in the utilization review process which intimately involves the state in the determination of the dispute concerning the injured worker's right to medical treatment through a state established procedure. The private decision to seek utilization review and to stop medical benefits, standing alone, cloaks defendants with no authority to interfere in an injured worker's receipt of benefits. The supersedeas cannot be initiated outside of the state's legal framework for utilization review and cannot be maintained without the Bureau's approval.

Thus, the employer's power over an injured worker's continued receipt of medical benefits does not begin and end with a "private" decision to invoke utilization review, as the Petitioners insist. This is not a situation in which a private decision is self-executing and can be carried out without entanglement or interaction with state procedures, state administrative machinery, and state officials. *See, e.g., Tulsa, supra.* The employer's power to supersede benefits emanates directly from the state and is dependent upon the state's approval at every key juncture.

Tulsa reinforces this conclusion. There, the Court rejected the argument that a non-claim statute was self-executing, and held that an executrix's statutory duty to file notice to creditors of the estate constituted state action because it involved the "overt, significant involvement of state officials." *Id.* at 486-87. Central to the Court's holding was the fact that, because the legal proceedings triggered the time bar, the legal proceedings themselves substantially

involved the state in the notice process and rendered the state and the private party joint actors for purposes of the Fourteenth Amendment. *Tulsa*, 485 U.S. at 487. *Accord National Collegiate Athletic Association v. Tarkanian*, 488 U.S. 179, 192 (1988) (state action exists where the "government has created a legal framework for the challenged conduct.").

Here, the decision to stop benefits, standing alone, has no legal effect without an application for admission to the state's utilization review process and approval by state officials. Like the non-claim statute in *Tulsa*, the request for utilization review triggers legal proceedings and within the context of those proceedings, "adversely affects" the injured worker's constitutionally protected interest. 485 U.S. at 491.

b. Traditional Government Function

The second factor identified in *Edmonson* is whether the private actor is engaged in a traditional government function. In the context of the Pennsylvania workers' compensation system, the provision of medical treatment to injured workers, the power to determine whether medical treatment is reasonable and necessary, and the power to stop or supersede those benefits after a determination that the treatment is not reasonable and necessary, have been exclusively within the province of the state. Injured workers must seek medical care for work related injuries through the state, and only through the state. The system is mandatory. Workers cannot opt-out of the system, pay for their own treatment, sue their employers for the cost of their treatment, nor sue the insurers for their failure to provide treatment. Injured workers have no choice but to rely on the state to fulfill its statutory obligation to them.

The constitutional import of this mandatory and exclusive state structure is set forth in *West*. There, the state was under both a constitutional and statutory obligation to provide medical care to inmates housed in state prisons. To fulfill this obligation, the state contracted with a private doctor to provide for medical care. The Court found the doctor to be a state actor because "in the prison context, medical care is the

'exclusive prerogative of the State' ". Thus, the doctor was a "willful participant in joint activity with the State." *Id.*, 487 U.S. at 47.

While Plaintiffs are not prisoners in the sense of *West*, they are nonetheless captives of the state system. Employers and insurers, like the doctor in *West*, are participants in a wholly state-created and administered public benefit system which has a legal obligation to provide medical care to beneficiaries who have no alternative source of such care. Employers and insurers, by virtue of their contract with employers, stand in the same relation to the state and the recipient of medical care as did the doctor in *West*. Here the state guarantees the delivery of medical care to the injured worker by imposing upon the employer the obligation to pay for it, either directly or through a contract of insurance.[28] The provision of workers' compensation benefits in Pennsylvania is, therefore, an exclusive state function.[29]

Power over the process of determining the reasonableness and necessity of medical treatment has historically been exclusively held by the state. Prior to the enactment of the 1993 Amendments, only a workers' compensation judge could make such a determination. *See, infra,* at 7-8. An injured worker's right to medical treatment could not be superseded until notice and a hearing had been provided. Indeed, having created a recognized property interest in medical treatment, the state was under a constitutional obligation to ensure that

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[28] Insurers' curious effort to distance themselves from employers under the Act, by pointing to their "voluntary" participation in the system and their contractual relation with the employer, is unavailing. Having decided to participate in the system, their obligations under the Act are identical to those of the employers. Their not so subtle threat to withdraw from this participation should they be deemed state actors should have no bearing on the state action analysis.

[29] This is not to say that Petitioners are necessarily state actors for all purposes under the Act. Plaintiffs have never made such a claim and the Court does not have to go that far to find that they are state actors in the context of utilization review.

the injured workers' receipt of that benefit was not interrupted without due process. *Logan, supra.*

Utilization review provides a dramatic departure from this practice. It delegates to employers the state's power to determine that treatment is unreasonable and unnecessary and to stop benefits on that basis, and thereby abdicates the state's responsibility to ensure due process in the administration of its public benefit program. The fact that a state delegates to a private party some of its power does not change the governmental character of the power exercised. *Edmonson*, 500 U.S. at 626. When they stop benefits pursuant to utilization review, employers are fulfilling a traditional,[30] if not exclusive, governmental function.[31]

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[30] The insurers' argument that the provision of workers' compensation benefits is not a traditional government function because the benefits are paid by the employer or the insurer, and not the state, misses the mark. The benefits are paid as a result of a statutory entitlement which substituted the no-fault compensation system for the forfeiture of the constitutional right of the employee to sue the employer in tort for workplace injuries. The fact that the state chose to fund the system through an employer mandate rather than an employer tax does not change the character of the benefit or its constitutionally protected status. It is the state through its police power which has conferred the benefit, not the employer. The insurers' analogies to car insurance, therefore, are completely inapposite. Car insurance is a requirement, not an entitlement. Like car insurance, employers are required to carry workers' compensation insurance. As to them, coverage is not a public benefit but a mandatory duty. Employees, however, stand on a completely different footing. Workers' compensation coverage for them is an entitlement and once they are deemed eligible, is one in which they have a constitutionally protected property interest which cannot be divested without due process of law.

[31] For purposes of the *Edmonson* analysis, it is not necessary to engage in the debate over whether the public function must be a traditionally exclusive one. *Edmonson* uses public function as a factor, not a test complete in and of itself, in a totality of the circumstances analysis, and does not address, much less answer, the question whether state action predicated upon a public function test, standing on its own, contains an exclusivity requirement.

c. Aggravation by Unique Incidents of Governmental Authority

Every injured worker receiving workers' compensation benefits is aware that those benefits emanate from the state. Some injured workers' benefits were determined by a workers' compensation judge through an adjudicative process in which the full panoply of state authority has been invoked to establish their entitlement. Their right to receive benefits is set forth in a decision by a workers' compensation judge or a judge from the state's appellate system, and carries with it the prestige and authority of a court order. Those injured workers whose benefits were decided by agreement are aware that those benefits are more than a matter of their employers' grace. Each agreement is documented upon a state form which sets forth the parameters of the injured worker's entitlement and is legally binding. Many of those agreements have been specifically approved by a workers' compensation judge.

The stoppage of benefits without notice or an opportunity to be heard in this context brings with it a betrayal of the trust which emanates from the state's guarantee of medical coverage, memorialized in state documents bearing the name of the Commonwealth of Pennsylvania and the Bureau of Workers' Compensation. The harm caused by the stoppage of benefits through utilization review is aggravated in a unique way by the context in which it occurs. Moreover, it can only occur through a legal framework established by the state itself. When injured workers call the Bureau to find out how their benefits could have been stopped without notice to them or an opportunity to defend themselves, they learn that the state has placed its imprimatur upon the employers' conduct and that they, as purported beneficiaries of the system, are powerless to rectify this injustice.[32] They also learn that the employer

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[32] Indeed, many claimants, including four of the named Plaintiffs, have had their medical benefits stopped through utilization review directly after a Request for Supersedeas hearing which was held within the context of a petition by their employer to terminate, suspend, or modify their benefits and at which a workers' compensation judge has denied

has been delegated authority to interfere with their state-sanctioned benefits without having to show any factual or medical justification. They are forced into, and then trapped in, a state utilization review process in which they are denied any opportunity to speak in their own defense or to have counsel speak on their behalf.

The injured workers' loss under these circumstances is clearly aggravated in a unique way by the mantle of governmental authority which has been bestowed upon their employer to stop their government entitlement. *United States v. Classic*, 313 U.S. 299 (1941). The harm goes beyond human suffering, in the form of physical pain and prolonged and exacerbated disability, to the very root of the due process clause itself, which serves not only to prevent mistaken and arbitrary deprivations of property, but to make the individual so deprived feel that his government has treated him fairly. *Richmond Newspapers, Inc. v. Virginia*, 448 U.S. 555, (1980); *Joint Anti-Fascist Refugee Committee v. McGrath*, 341 U.S. 123, 172 (1951) (Frankfurter, concurring). The deprivation of medical care without notice, with no pre-deprivation opportunity to be heard, and the exclusion of the injured worker from the utilization review process until the appellate stage of review which occurs at the very least, months after the

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supersedeas and ordered that benefits be continued. *See* Jnt. App. at ¶¶ 96-99, 111-113, 147-150, 249-252. Request for supersedeas hearings were put into place by the Consent Decree in *Baksalary* to replace the automatic supersedeas provision invalidated in that case. That the employer can effectively ignore the judge's decision undermines the constitutional remedy which was devised after ten years of litigation in *Baksalary* and justifiably shakes a claimant's confidence and respect for the system and for the authority of the workers' compensation judge who will decide his/her case. A claimant can have little confidence in the fairness of a system in which a supposedly co-equal litigant in the proceedings can vitiate the judge's decision and revoke the benefits the judge has specifically ordered to continue.

medical treatment has been stopped, is inconsistent with these important constitutional principles.[33]

d. The Third Circuit Properly Applied the *Edmonson* Factors

Contrary to the Petitioners' accusation, the Third Circuit's decision, which took into account the totality of the circumstances surrounding the insurers' participation with the state in the provision of workers' compensation benefits generally, and the supersedeas of those benefits which is at the heart of this case, was in accordance with a coherent theory of state action and completely consistent with this Court's decision in *Edmonson*. Far from being miscellaneous irrelevancies, as the Petitioners charge, the factual context used by the court was necessary to place the role of the insurers in the state system in its proper perspective. The picture which emerges when all the relevant factors are considered dictate that the Third Circuit's finding of state action be affirmed.

B. EVEN IF DISCRETE TESTS ARE REQUIRED, THE THIRD CIRCUIT'S STATE ACTION HOLDING AGAINST THE INSURERS SHOULD BE AFFIRMED

1. Joint Participation/Symbiotic Relationship Test

The joint participation/symbiotic relationship test was first identified in *Burton v. Wilmington Parking Authority*, 365 U.S. 715 (1961). There, the Court looked to the many interactions between the state and private restaurant owner who leased space in a state owned facility and attributed particular significance to the fact that both the restaurant and

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[33] Although, since the Third Circuit's Decision, the state has changed its procedures to allow injured workers to submit a personal statement during utilization review, the Petitioners are asking the Court to declare that it would be constitutional, should the state decide to change its procedures, to defer this opportunity until *after* the benefits have been stopped.

the state benefitted economically from the restaurant's decision to practice discrimination. The state and the restaurant were found to be joint participants in the discriminatory activity, notwithstanding the fact that the restaurant chose on its own, without consultation with the state, to discriminate on the basis of race.

The Court has applied this analysis to find state action in other contexts as well. In *Lugar*, for instance, the court found state action in Virginia's prejudgment attachment procedures. There, a creditor executed an *ex parte* affidavit alleging a belief that the debtor might dispose of his property in order to defeat his creditors. That decision was a private one, made without consultation with state officials. Acting on this allegation, the Clerk of the state court issued a writ as a matter of course which was then executed by the County sheriff. The Court held that private use of state procedures with the help of state officials to accomplish a prejudgment deprivation of a constitutionally protected property interest constitutes state action. The Petitioners' emphasis on the fact that they decide to invoke utilization review without consultation with the state is as misplaced and irrelevant here as it was in *Burton* and *Lugar*. For purposes of establishing a symbiotic relationship, the focus is upon the interaction between the state and the employer, the joint motivation underlying the challenged conduct, and the mutual benefit derived by both the state and the employer when the utilization review process is invoked.

Many of the factors set forth in Section III (A)(2)(b), *infra*, under the first *Edmonson* principle, are relevant to whether the employers and insurers act in joint participation with, or in a symbiotic relationship with the state, when they invoke utilization review and stop workers' compensation medical benefits on that basis. The interconnection between the state and the employers in that process is a critical factor in the analysis. No employer may stop benefits without properly invoking the utilization review procedures and enlisting the state to approve its request. Only if that request is granted and the utilization review is permitted can the supersedeas be legally maintained. Thus, this situation is closely akin to the statutory mechanism invalidated in *Lugar*. Here, while the

Bureau employs no sheriffs to assist employers in confiscating the challenged property, the property in dispute, and to which the injured worker presumptively has an entitlement until due process is afforded, is sequestered by the employers with the full knowledge, participation, and imprimatur of state officials.

There is no dispute that the utilization review procedures at issue here were legislated by the state, at the behest of the employers and their insurers, to contain medical costs in the workers' compensation system. The state's policy of cost containment was intended to further its own interest in attracting business to Pennsylvania.[34] To ensure that its own interest was achieved, the statute ensured that employers and their insurers would derive economic benefit directly from the utilization review provisions, who stand to save money each time they invoke the process, whether or not their challenge to the medical treatment under review is ultimately successful.[35]

The state's interest is likewise furthered every time an employer invokes the utilization review procedures and stops benefits. Indeed, if employers did not do so, the interests the state sought to advance through the statute would never be realized. So important to the state is the cost savings to the employers, and so intertwined are the state's and the employers' interests, that the Bureau maintains an office, staffed by state employees, whose specific purpose is to contain the costs of the employers and their insurers.[36] The employer's decision to invoke review in any particular case,

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[34] *See* Third Circuit Brief of Commonwealth Appellees, at 16. *See also* Brief for Petitioners at 44-45.

[35] Because injured workers cannot pay for services pending the review, no matter how legitimate their need for continued treatment or how long the initial review and the appellate process might drag on, there is nothing, in most cases, for the employers to reimburse even if the treatment is ultimately deemed to be reasonable and necessary.

[36] *See* Third Circuit Appendix, Deposition of David Weyl, Chief of Bureau's Cost Containment Unit at B-135, responding to the question, "Whose costs do you contain?": "We are containing the medical costs incurred by employers and insurers, if they have insurers".

therefore, is inevitably intertwined with the state's interest, even though the state is not consulted in advance.

In this situation, therefore, the evidence of joint endeavor by the state and the employers is far stronger than it was in *Burton* or *Lugar*. In *Burton* the state expressed no direct policy interest in the discrimination which was practiced by the restaurant. It was a passive recipient of the increased business generated by the restaurant owner, but there was no evidence that the state was even aware that the restaurant's policy existed. The economic benefit derived by the state through the restaurant's discriminatory conduct was not in furtherance of any expressed policy of the state. The same is true in *Lugar*, where the state provided the procedural scheme utilized by the defendant with the assistance of state officials, but remained neutral as to whether or not the statute was utilized.

Blum v. Yaretsky is not to the contrary. There, the state was not involved in the utilization review process used to assess and diminish the level of care provided to patients within a private nursing home. Although the utilization review was undertaken in accordance with state regulations, and the state was ultimately notified about the action taken by the nursing home and adjusted the payment to the nursing home accordingly, there was absolutely no interaction with the state until the decision to perform utilization review had been made, the review completed, and the ultimate decision as to the appropriate level of care determined. The procedures were entirely self-executing, *i.e.*, they were invoked and utilized by the private nursing home without any state involvement. The activity of the nursing home and the state operated in separate, self-contained spheres which touched, but never intersected. Additionally, in *Blum* there was no challenge to the constitutionality of the procedures themselves. The Plaintiffs in *Blum* never challenged the reduction of their benefit, only the medical decision by their treating doctors as to the level of care they would receive.

This case could not be more different. Here, it is not an institutionally internal medical decision which is being challenged, but the state procedure which permits an employer, in accordance with an express state policy of cost containment, to

override a private doctor's medical decision that treatment is reasonable and necessary. Far from being self-executing, the supersedeas of benefits can be invoked only through an established state procedure which requires interaction between the state and the employer or insurer seeking review. It advances an express policy of the state to benefit both the state and the employers economically. Based on this Court's decisions in *Burton* and *Lugar* there is a symbiotic relationship and joint participation between the state and the employers when benefits are stopped under utilization review.

2. The Public Function Test

The facts set forth in the *Edmonson* public function analysis, *see infra*, at III(A)(2)(b), are sufficient in and of themselves to establish the employers' liability as state actors under the public function test espoused by Petitioners. The only question remaining is whether the power to stop an injured worker's benefits pursuant to utilization review is a function which has heretofore been an exclusive state function, or, more to the point, whether exclusivity ought to be relevant to the analysis at all.

Prior to *Edmonson*, the public function test as articulated by the Court had required that the function delegated to the private party be one traditionally and exclusively performed by the state. *See Flagg Brothers*, 436 U.S. at 157-160. After *Edmonson* much debate ensued as to whether or not the public function test still required exclusivity. *Edmonson* did not use the word "exclusive", a point which was hotly attacked in the dissent. 500 U.S. at 640. Some courts and commentators since *Edmonson* have opined that the exclusivity requirement was eliminated from the public function test, *e.g., Mark v. Borough of Hatboro*, 51 F.3d 1137 (3rd Cir.1995) (Greenberg, concurring); *McKeesport Hospital v. Accreditation Council*, 24 F.3d 519 (3rd Cir. 1994) (Becker, concurring), while others have treated the absence of the exclusivity language in *Edmonson* as a mere oversight on the part of the Court. *E.g., United Auto Workers v. Gaston Festivals, Inc.*, 43 F.3d 902, 906 (4th Cir. 1995); *Gallagher v. Neil Young Freedom Concert*, 49 F.3d 1442 (10th Cir. 1995).

As stated previously, this debate fails to perceive that in *Edmonson*, public function was identified as one of several factors or guiding principles to be utilized in a balancing analysis, not as a "test" which by itself would identify the presence or absence of state action. *See infra*, III(A)(1). Accordingly, it was not necessary to determine whether, if a public function test standing alone exists after *Edmonson*, exclusivity would still be required.

Here, the state has had exclusive control over the stoppage of an injured worker's medical benefits since 1984. Without the consent of an injured worker or an Order of a workers' compensation judge, those benefits were required to continue. Even if exclusivity is required, therefore, Plaintiffs satisfy the test.

The Court has stated, however, that a function does not satisfy the exclusivity test unless it is "traditionally" an exclusive state function. Petitioners respectfully contend that the exclusivity requirement, as articulated in *Flagg Brothers*, is not an element which properly belongs in the public function analysis.

This Court has concluded that to identify the attributes of a traditional governmental function is an impossible task. *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528, 544 (1985).[37] To identify one which has been historically exclusive is even more daunting than the task abandoned by the Court in *Garcia*. As the Court observed there, it is impossible to consistently apply such a requirement because what is a traditional or exclusively governmental function has changed as our society has developed. 469 U.S. at 543. Particularly since the New Deal, the government has taken responsibility for many functions which were previously performed by the

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[37] *See also Reitman v. Mulkey*, 377 U.S. at 378 (characterizing as an "impossible task" the formulation of an infallible test for determining whether the state, in any of its manifestations, has become significantly involved in private discriminations).

private sector. To require traditional exclusivity in the public function doctrine would force courts to ignore contemporary experience and would in effect "freeze into law a static conception of Government." *San Francisco Arts and Athletics v. United States Olympic Committee*, 483 U.S. 522, 549 n.1 (1987) (Brennan, *dissenting*). This would permit the exclusion from scrutiny of numerous activities in which the state has exclusively occupied a field of endeavor and then delegated that function to a private entity. Constitutional scrutiny could then be evaded by a private entity, despite its acceptance of a power previously exercised only by the state, if it can point to an earlier time in which the function was privately administered. There would be no limit to how far back a defendant could reach to avoid application of the public function doctrine. In this age of privatization of traditional governmental duties and responsibilities such a result would be unacceptable, as it would allow the state to avoid the strictures of the Constitution by simply ceding its duty and power to a private entity. If the Court maintains a free-standing public function analysis, and within that test an exclusivity requirement, it should deem exclusivity to be satisfied by evidence that the state exclusively occupied a field of endeavor at the time it delegated the function to the private entity.

Even if the Court continues to require traditional exclusivity as part of the public function analysis, however, it would be inappropriate to apply it to this case. Since 1984 in Pennsylvania, the state has exclusively reserved to itself the power to stop an injured worker's medical benefits. Prior to that time, employers were permitted to stop them pursuant to a procedure very like the one at issue here. That provision, however, Section 413 (a) of the Act, was deemed unconstitutional in *Baksalary, supra*. An inflexible application of the exclusivity requirement would permit employers to avoid scrutiny under the public function doctrine because the state, in the past, permitted them to exercise power unconstitutionally.[38] Such a

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[38] The insurers cite to *Silas v. Smith*, 361 F. Supp. 1187 (E.D. Pa. 1973) and *Henderson v. Workers' Compensation Appeal Board*, 69 Pa. 613, 452 A.2d 277 (1982), but fail to disclose that both cases were effectively overruled by *Baksalary*. The consent decree which resulted in that case vested the state with the exclusive right to stop medical benefits.

result should be emphatically rejected, as it would not further the goals of the public function analysis, and would surely produce a constitutional anomaly.

3. Government Compulsion and Encouragement

The third "test" relied upon by the Petitioners is the government compulsion test. This argument is somewhat disingenuous because the Court has never required compulsion to find state action. If the state has provided such significant encouragement, either overt or covert, that the choice exercised by the private actor must be deemed in law to be that of the state itself, state action is present. *Blum v. Yaretsky*, 457 U.S. 991, 1004 (1982); *Jackson v. Metropolitan Edison Company, supra*.

Plaintiffs do not disagree that state encouragement or compulsion requires more than intensive state regulation. They have never contended that the insurers, who, to be sure, are extensively regulated by the state, are state actors for that reason alone. *Blum, supra*; *Moose Lodge No. 107 v. Irvis*, 407 U.S. 163 (1972).

In order to escape the appearance of any nexus to the state, Petitioners attempt to place the decision to invoke utilization review in a vacuum, as if it were that decision alone, outside of the state's established system for review of reasonableness and necessity of medical treatment, which causes the harm of which the Plaintiffs complain in this case.

While it is true that the state does not preview each request for utilization review, the statutory scheme clearly encourages the use of the utilization review process and the supersedeas of benefits which it authorizes. The Act prohibits an employer from unilaterally stopping an injured worker's medical benefits except in the context of utilization review. By granting them the power to stop benefits in that unique

context, the state is furthering its expressed policy of cost containment.

This Court has recognized that state encouragement of an ostensibly private decision may take subtle forms. In *Reitman, supra*, for instance, the Court found state action on the part of an individual who had used a facially neutral state constitutional amendment which had the purpose and effect of authorizing, but not mandating, racial discrimination in the housing market. The Court looked to the immediate objective of the legislation, the ultimate effect, and the historical context to determine that the state was using the amendment to encourage private discrimination, something which it could not do directly. By deputizing private citizens to advance the state's agenda, the individuals who carried that agenda forward through their use of the amendment became state actors.

The Amendments at issue here, which permit, but do not require, the insurers to stop an injured worker's state entitlement to medical benefits without notice or an opportunity to be heard, had the purpose and effect of encouraging the insurers to do indirectly what the state could not do directly, that is, to stop injured workers' access to medical care without pre-deprivation process. The immediate objective of the legislation was to contain costs in the state's workers' compensation program. To achieve the objective of this express state policy, the state enlisted employers and insurers to advance its purpose. It focused the attention of the employers on the reasonableness and necessity of medical treatment, the direct target of the state's cost containment effort, and permitted employers to stop those benefits through the utilization review process, and only that process.[39] It imposed no criteria to protect an injured worker from the arbitrary stoppage of his benefits and ensured that the consequences to the employer

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[39] Thus, here there is even more evidence of state action than was present in *Reitman*, because there, the individual was free to discriminate on any ground he chose. *See Alliance for Community Media v. FCC, supra*, (applying *Reitman* analysis to find government encouragement of suppression of indecent material, something which the government could not do directly, through the acts of private cable operators).

for erroneous or unfounded use of the process would be minimal, by precluding an injured worker from securing the challenged treatment pending review.[40] In short, by invoking utilization review, the insurer had everything to gain and nothing to lose, a fact which was sure to encourage widespread use of the process. Indeed, by January of 1995, when this case was filed, and just sixteen months after the law went into effect, more than 40,000 requests for utilization had been filed. Jnt. App. at 16.

Unlike this case, in which the state had an express policy of cost containment which it advanced by deputizing employers to stop medical benefits, the cases cited by the Petitioners to avoid a finding of state encouragement or compulsion are inapposite. In *Jackson*, for instance, while the private utility had been granted a monopoly and was a heavily regulated business, the state had no policy, rule, or procedure concerning the termination of services. The state's regulation of the utility was unrelated to the transaction which gave rise to the constitutional dispute. *Accord Rendell-Baker v. Kohn, supra* (regulation imposed by the state upon the private school was unrelated to the personnel action which formed the basis of the constitutional challenge). Additionally, the decision to terminate services was self-executing and did not require the participation of state officials. In terminating services, the utility was not exercising any authority or power delegated by the state.

Likewise, in *Flagg Brothers*, the only state involvement was the passage of a statute that regulated private conduct. The state provided a mechanism for resolution of private disputes but had no contact whatsoever with the private parties who used it. The statute was wholly self-executing and the state was completely neutral as to whether the procedures

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[40] The insurers' and the DOJ's observation that the 10% penalties discourage arbitrary use of the process is disingenuous at best, since 10% of nothing is 0. Unless an injured worker can convince her medical provider to treat him gratuitously during the review process, which can take years to complete if appeals are involved, the injured worker is precluded from generating bills which would call for reimbursement.

were utilized. It did nothing to encourage the use of those procedures and derived no benefit from their use.

Here the state procedures under challenge were designed to and did in fact encourage the employers to interfere in the injured workers' property interest in the receipt of medical treatment. The fact that employers voluntarily used those procedures without advance consultation with the state, something upon which the state depends for the advancement of its cost containment agenda, does not diminish the state's role in the employer's conduct, but rather, increases it.[41] Employers in this context are state actors.[42]

CONCLUSION

For all the reasons stated herein, Respondents respectfully urge the Court to affirm the decision of the Court of Appeals for the Third Circuit.

Respectfully submitted,

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[41] *See Reitman*, 387 U.S. at 381-87 (Douglas, concurring); *see also Alliance Media, supra*, 10 F.3d at 822 n.13.

[42] Plaintiffs note that the Petitioners rely upon numerous facts and statistics which were not in the record in the district court. It must be remembered that Plaintiffs' due process challenge was dismissed pursuant to a motion under 12(b)(6) of Federal Rules of Civil Procedure. Thus, the facts as Plaintiffs have alleged them govern the analysis of this case.